DOCUMENT RESUME

ED 074 884 HE 003 682

AUTHOR	Woodhall, Maureen
TITLE	Financing Students in Higher Education: Educational, Social and Economic Implications of Alternative Methods of Finance.
INSTITUTION	United Nations Educational, Scientific, and Cultural Organization, Paris (France). International Inst. for Educational Planning.
REPORT NO	IIEP-TM-42-69
PUB DATE	[69]
NOTE	13p.; Paper in The Fundamentals of Educational Planning: Lecture-Discussion Series
EDRS PRICE	MF-$0.65 HC-$3.29
DESCRIPTORS	*Educational Finance; *Educational Planning; Financial Support; *Higher Education; Public Support; *Scholarship Loans; Student Costs; *Student Loan Programs

ABSTRACT

This lecture is part of "Fundamentals of Educational Planning; Lecture-Discussion Series," a controlled experiment aiming at the development of efficient teaching materials in the field of educational planning. The author discusses (1) the justification for public subsidy of higher education; (2) methods of subsidizing students; (3) the objective of student aid programs; (4) grants versus loans for students; and (5) the evaluation of systems of student aid. In addition, reading materials are suggested for those who wish to pursue the topic further. (HS)

FILMED FROM BEST AVAILABLE COPY

ED 074884

The Fundamentals of Educational Planning : Lecture - Discussion Series

---

No. 42 FINANCING STUDENTS IN HIGHER EDUCATION:
EDUCATIONAL, SOCIAL AND ECONOMIC IMPLICATIONS
OF ALTERNATIVE METHODS OF FINANCE

by Maureen Woodhall

U.S. DEPARTMENT OF HEALTH,
EDUCATION & WELFARE
OFFICE OF EDUCATION
THIS DOCUMENT HAS BEEN REPRODUCED EXACTLY AS RECEIVED FROM THE PERSON OR ORGANIZATION ORIGINATING IT. POINTS OF VIEW OR OPINIONS STATED DO NOT NECESSARILY REPRESENT OFFICIAL OFFICE OF EDUCATION POSITION OR POLICY

IIEP/36.42

Unesco : International Institute for Educational Planning

ED 074884

IIEP/TM/42/69

INTERNATIONAL INSTITUTE FOR EDUCATIONAL PLANNING
9, rue Eugène Delacroix
Paris 16e, France

FINANCING STUDENTS IN HIGHER EDUCATION: EDUCATIONAL, SOCIAL AND ECONOMIC IMPLICATIONS OF ALTERNATIVE METHODS OF FINANCE

by

Maureen Woodhall

This lecture is part of 'Fundamentals of Educational Planning; Lecture-Discussion Series' a controlled experiment undertaken by the International Institute for Educational Planning in collaboration with a limited number of organizations and individuals aiming at the development of efficient teaching materials in the field of educational planning. By their very nature these materials, which draw upon tape recordings, transcriptions and summary notes of seminars, lectures and discussions conducted by IIEP as part of its training and research programme, are informal and not subject to the type of editing customary for published documents. They are therefore not to be considered as 'official publications'.

The opinions expressed in this lecture are those of the author and do not necessarily represent the views of the Institute.

CONTENTS

		Page
1.	The justification for public subsidy of higher education	1
2.	Methods of subsidizing students	3
3.	The objective of student aid programmes	4
4.	Grants versus loans for students	6
5.	The evaluation of systems of student aid	8
	Suggested Additional Reading	10

1. The justification for public subsidy of higher education

In recent years the rapid expansion of higher education throughout the world has emphasized the problems of financing the most expensive level of education. Costs per student in higher education tend to be very much higher than costs per pupil at any other level of education. In most countries higher education is financed by a combination of public and private sources of funds. Even if universities do not charge tuition fees, the student himself normally bears a considerable part of the total resource cost of education in the form of the earnings forgone while he continues his education, instead of joining the labour market. These forgone earnings represent one of the costs of higher education both to the individual - who loses income he would have received if he were not a student - and to the community - which loses the output the student would have produced if he had joined the labour market. On the other hand, even if universities do charge fees these generally do not represent the full costs of tuition, so that some form of subsidy is required to finance the current and capital expenditure of universities.

The question of how higher education should be financed, and what should be the balance between public and private contributions raises a number of issues. For example, what level and form should public subsidy of education take and what is the justification for this subsidy; should financial assistance be given directly to institutions of higher education, to enable them to reduce or abolish fees, or to students, to enable them to pay fees; should public subsidies for higher education be financed out of general taxation or in some other way? This paper is concerned with the issue of financial aid for students: what are the objectives of student aid schemes in different countries; what form and level does financial assistance take; what are the criteria for selecting students for aid; and finally how should alternative systems of student aid be evaluated?

But since financial aid to students is only one form of public subsidy of higher education, it is interesting to consider first the justification for subsidization of higher education out of public funds. The main economic justification for providing public finance for any service is that society as a whole derives some benefit from the service, and that provision would be neglected or reduced if it were left entirely to private individuals to finance it. Thus subsidy of higher education is justified by the argument that it produces both economic and social benefits for society, including highly qualified manpower, cultural and aesthetic values, additions to human knowledge, and so on. It is recognised that higher education also produces direct economic and non-economic benefits for the educated individuals themselves, but the case for public subsidy rests on the belief that the benefits to society exceed the benefits to individuals.

There is another argument for public subsidy of higher education. If opportunities for higher education were given only to those who could afford to pay for it, it would be both inefficient and inequitable. It would be inefficient because some of the most able students would not be able to afford to continue their education, and it would be inequitable because higher education confers benefits on the individual in the form of better job opportunities and higher lifetime earnings, so that to distribute education in accordance with individuals' purchasing power would mean preserving and exaggerating inequalities of income in the future.

Thus the subsidy of higher education out of public funds has both an economic and a social justification. The next question that must be answered is what form the subsidy should take, and how it should be financed. The following table summarizes various possible ways of subsidizing higher education.

Table 1. Alternative methods of financing and subsidizing higher education

Methods of subsidy	Methods of financing
1. Direct subsidy to institutions to eliminate or reduce fees	1. General taxation of income (at central or local level)
2. Direct subsidy to students in the form of unconditional grants	2. General taxation of expenditure e.g. sales tax, excise duties (at central or local level)
3. Direct subsidy to selected students in the form of means-tested grants, scholarships or bursaries	3. Special taxation of graduates' incomes
4. Direct subsidy to students in the form of guaranteed loans at interest rates below market rates	4. Loan repayments of past students
5. Direct subsidy to students in the form of specially provided part-time paid employment or meals and accommodation at prices below market prices	
6. Direct subsidy to parents or to graduates in employment, in the form of tax concessions for educational expenditures	

2. Methods of subsidizing students

Most countries subsidize higher education by means of a combination of direct payments to institutions, to cover capital and current expenses, and payments to some individual students, to cover fees where necessary, and also living expenses. The payments to students take different forms in different countries. Many countries, both developed and developing, have scholarship schemes under which grants are made to selected students, chosen either on the basis of ability or of financial need. These grants are sometimes unconditional, as for example in the United Kingdom, where all students who gain admission to a university are eligible for consideration for a grant, although the amount a student receives is subject to a means test, and thus determined by the level of his parents' income. Alternatively, the grant may be subject to certain conditions, for example in Ghana students receive grants on the condition that they work for the government on graduation.

A number of countries, both developed and developing, give some aid to students in the form of repayable loans, with or without interest, rather than outright grants. Loans now constitute some part of the finance of higher education in at least ten advanced countries, U.S.A., Canada, Japan, Australia, Sweden, Norway, Denmark, Finland, Western Germany and the Netherlands, and a number of developing countries, including India, Kenya, Colombia, Venezuela, Peru and the Dominican Republic.

Another form of financial assistance to students is specially provided part-time paid employment. Many American universities have for some time operated private schemes of this sort, and in 1964 the Federal Government set up the College Work-Study Programme, which provides Federal funds to colleges and universities to enable them to expand job opportunities for students.

The proportion of students receiving direct aid varies considerably between countries. In some developing countries less than 3 per cent of students in higher education receive any form of scholarship, whereas in the U.K. and Scandinavian countries over 70 per cent of students receive some direct aid. A survey carried out in 1959-60 for the International Study of University Admissions showed that taking all countries together, 32.9 per cent of students in higher education in developed countries received direct aid, and 8.7 per cent in less developed countries. Table 2 summarizes the proportion of students receiving aid in 40 countries.

Table 2. Percentage of students receiving direct aid in various countries

	Nil	0-3	4-8	9-15	16-30	31-50	51-100
Developed countries	1	3	5	1	1	0	1
Less developed countries	6	11	4	2	3	1	1
Total	7	14	9	3	4	1	2

Finally, most countries provide indirect subsidies to students, as well as making some direct payments. It is difficult to obtain accurate data on levels of expenditure on indirect aid, since it is sometimes financed by ministries other than the Ministry of Education, but no review of financial aid to students would be complete without consideration of expenditure on housing, food and travel subsidies and medical and welfare expenditures.

3. The objectives of student aid programmes

Student aid schemes in different countries may have a number of different objectives. The International Study of University Admissions, conducted by Unesco and the International Association of Universities, included a brief review of financial aid schemes for students, and classified the schemes into four main categories:

(a) 'seed-bed' schemes, generally found in the poorest and educationally most backward countries. Such schemes provide aid for a handful of students, and their main purpose is to promote a rapid expansion of education at a later date;

(b) 'manpower' schemes, whose chief aim is to provide aid to meet a country's requirements for various types of skilled manpower;

(c) 'equalization' schemes, which are concerned with increasing and equalising educational opportunities, and their main purpose is to ensure that no able student is prevented from continuing his education by financial need;

(d) 'salary' schemes, under which aid is given to all students, regardless of their own or their parents' means, and thus aid becomes, in effect a salary paid by the State to all students.

These four categories demonstrate that different student aid schemes may be intended to fulfill different objectives. For example, the objective of 'manpower' schemes is primarily economic, while 'equalisation' schemes have a mainly social justification. This method of classification is illuminating but unfortunately there are few student aid schemes that can be neatly classified in terms of a single category. In most countries, student aid policy has a number of different objectives, including economic, social and educational aims. When administrators of State student aid schemes are asked what is the main purpose of student aid, they may reply 'to encourage demand for education' or 'to equalise educational opportunities', 'to ensure a sufficient supply of highly qualified manpower for the labour force' or 'to allow students to use their time in the most instructive way, so that they are not forced to work part time or to interrupt their studies, because of financial difficulties'. In fact, in most countries student aid is intended to satisfy all these objectives at once, which makes it difficult to evaluate fully most student aid schemes, because their aims are so diverse.

For example, in the U.S.A. there are two State subsidized loan schemes for university students, the National Defense Student Loan Program and the Guaranteed Loan Program for Higher Education. The purpose of these schemes is to provide low interest loans for students in low-income or middle-income families, to enable them to continue their education. Thus one of the main objectives of the scheme is the equalisation of educational opportunity. But one particular characteristic of the National Defense Student Loan Program has an economic justification: to encourage graduates to enter the teaching profession, in order to overcome a teacher shortage. Graduates who do enter teaching are forgiven part of the repayment obligation; any teacher has 10 per cent of his loan repayment obligation cancelled for each year of service as a full-time teacher, while teachers in low-income areas, or teachers of handicapped children have 15 per cent cancelled for each year's service. Thus, this particular student aid scheme has both an 'equalisation' and a 'manpower' element.

The fact that student aid schemes have many different objectives is very important when attempting to evaluate the effectiveness of student aid policy. If the aim of financial assistance is simply to increase demand for higher education, a first assessment of its effectiveness can be made by looking at enrolment figures. But if the aim of student aid is to equalise opportunity it is necessary to have information on the social class background of students, and to examine trends in social class participation rates in higher education. The effect of student aid policy on educational efficiency must also be judged in the light of the effects of financial assistance on students' propensity to part time work, on the average length of study and on wastage rates in higher education. Thus any student aid policy must be evaluated in terms of its economic, social and educational implications. In the following section we will examine some of the implications of two alternative methods of subsidizing students: by means of outright grants and scholarships, or by means of repayable loans.

4. Grants versus loans for students

Loans have been justified by some writers as a means of financing students for a number of reasons. At the same time other writers have attacked the idea of loans, and argued for a system of outright grants. The arguments can be briefly summarized under five headings:

(a) The supply of finance for higher education

Economists in Britain and the U.S.A. have argued for the use of loans to finance students on the grounds that this will increase the overall supply of finance for higher education. In the short-run it makes little difference whether financial aid is given in the form of grants or loans, since funds must be found to make the initial payments to students. On the other hand in the long-run there is a saving of public funds if the student is required to repay all or part of the loan. The extent of the saving depends on the period of time which graduates are allowed, in order to repay, and the interest which they must pay. Many loan schemes, for example in Scandinavia, provide interest free or low interest loans. In Denmark, for example, students receive aid in the form of 50 per cent grant, 50 per cent interest-free loan; in Norway, interest is charged at 4 3/4 per cent. Thus the saving involved in the loan scheme is less than if full commercial rates of interest were charged, but some saving of public funds is nevertheless achieved. Another possible way in which a loan scheme may increase the supply of finance for higher education is by tapping private sources of finance. For example, in Finland, and in the U.S.A. under the Guaranteed Loan Program, the initial loan for a student is provided by private banks, but under a government guarantee. In such cases the government subsidizes the interest on the loan, and meets the cost of cancellation of loans in cases of hardship or illness, or in the event of a graduate defaulting, but public funds are not required to finance the initial payments to students. Thus loans are often justified as a means of overcoming one of the long-term constraints on the development of student aid: a shortage of public revenue.

(b) The benefits of higher education

Advocates of loans argue that since higher education confers financial benefits on the educated, graduates should repay part of the cost of their education out of the higher lifetime earnings they enjoy as a result of this education. On the other hand advocates of grants frequently argue that society as a whole benefits in both economic and non-economic terms, from higher education, and the supply of highly qualified manpower, so that society as a whole should finance higher education out of general taxation. In fact the 'benefit' principle of taxation: that he who benefits from a service should provide the finance for that service can be used to support private payments and public subsidy, since higher education provides benefits both for the individual and for society. In Colombia, the Colombian Institute for Advanced Training Abroad (ICETEX) which administers aid for students in

higher education both in Colombia and abroad, gives loans rather than scholarships, on the grounds that 'education is good business, the profit reaped by the student being commensurate with the capital invested'. On the other hand many scholarship schemes are justified in terms of the contribution made by highly qualified graduates to national income, the country's need for qualified manpower, and the indirect or 'spillover' benefits generated by investment in higher education. The disagreement between advocates of loans and of grants is essentially over the degree of subsidy required to ensure optimum investment in higher education from the point of view of society.

(c) Equity and equality of opportunity

Closely linked with arguments about the benefits of higher education are arguments about the equity of alternative methods of finance. Loan advocates argue that loans are more equitable than grants, since graduates, who earn more than average as a result of their education, provide finance themselves, by repaying loans out of these higher than average earnings, whereas a grant scheme involves a transfer of income from the general taxpayer with average or below average earnings to those who will have high lifetime earnings. On the other hand opponents of loans argue that the need to repay loans will discourage working class students from entering higher education, and that grants will be more successful in equalising educational opportunity.

(d) The efficiency of higher education

Grants are often justified on the grounds that freedom from financial worry allows the student to work hard, and that fears of incurring large debts may force students to take up part-time work or even to drop out of higher education before completing their courses. In fact part-time work among students is a common phenomenon in many countries, but explanations for this are closely linked with the way university courses are organised, the length of time needed for a degree and similar characteristics in the structure of higher education. There is little direct evidence on the relationship between methods of financing students, and length of study or patterns of part-time employment.

(e) Practical problems of administering a loan scheme

Sometimes loans are attacked as unfeasible because of certain practical difficulties in implementing a loan scheme. For example, how is it possible to make concessions to graduates who have low incomes as a result of illness, unemployment, or the choice of low-income occupations? How is the problem of the married woman graduate who gives up working, to be solved? How will the authorities solve such problems as non-repayment by defaulters, or by graduates who emigrate? In fact, those countries that have adopted loan schemes have not found such problems to be insuperable. Most loan schemes include some element of 'insurance', so that graduates are permitted to

postpone repayment in the case of financial hardship. It is true that a loan scheme requires an efficient administrative structure to ensure that repayments are made regularly, and to deal with cases of hardship. But in Scandinavia the costs of administering the official loan schemes amount to only between 1 and 2 per cent of the total annual expenditure by the government on student aid.

5. The evaluation of systems of student aid

The aim of this brief paper has been to demonstrate that student aid policy in different countries is intended to satisfy many different objectives, and to show that there are alternative means of providing financial aid for students. Scholarships constitute one, but by no means the only, way of giving direct financial assistance to students. Loans represent a feasible alternative, and in some cases appear to be successful in increasing the supply of finance for higher education. But it is sometimes claimed that this is at the expense of certain undesirable consequences, particularly in discouraging working class students. In fact the reasons for low working class participation in higher education are extremely complex, and the structure of the educational system, methods of selection, and traditional attitudes must be analysed as well as methods of finance.

In order to evaluate loans as a method of financing higher education information would be needed on such issues as:

(i) What is the extent of public subsidy of higher education?

(ii) What is the stated justification for this degree of subsidy?

(iii) Has there been any attempt to estimate the private and social benefits of education?

(iv) What are the conditions of eligibility for loans?

(v) What are the terms of repayment?

(vi) What is the average level of debt of university graduates, at the end of their course?

(vii) What is the extent of part-time employment among students?
What evidence is there of the effect of loans on part-time employment?

(viii) What alternative forms of finance are utilised by students?

(ix) What is the average length of study and rate of wastage among students? What evidence is there of the effect of loans on wastage or length of study?

(x) What is the social composition of the student body?

(xi) What is the sex composition of the student body?

(xii) What evidence is there on the attitudes of women or working-class students to loans?

(xiii) Are special concessions given to graduates with low incomes or to married women?

(xiv) What are the general attitudes of students towards loans?

(xv) What are the costs of administration?

(xvi) What are the practical problems of administration in a student loan scheme?

(xvii) Are there any built-in flexibilities in the scheme, such as favourable repayment terms for particular groups of graduates?

(xviii) What are the financial savings produced by a loans scheme?

(xix) What have been the effects of changes in the method of financing?

(xx) What proposals for reform of the finance of higher education have been put forward?

These data would then need to be compared with similar data for a country operating a grant scheme, as opposed to a loan scheme for students. It would then be possible to evaluate loans and grants in terms of the objectives of student aid policy in each country.

Such an evaluation would require a major research project. Some information is available on loan schemes in the U.S.A. and Scandinavia, and is given in the bibliography. But a full evaluation of alternative methods of finance requires more information than is yet available.

However, the educational planner may gain some insights about the relative merits of alternative methods of finance by analysing the objectives of student aid in his own country. The International Study of University Admissions concluded its review of student aid with the observation:

> 'Few countries have decided what their aid programmes should achieve. It is still rarer for this to be done in any detail - on the basis of manpower studies, for instance. Administrative failures and the position of aid as the poor relation among educational problems have also meant that rarely has the best possible use been made of the limited funds available. Aid schemes cannot be expected to promote a country's educational, economic or social development efficiency if, as at present, no basis for their assessment and evaluation exists'.

Some progress has been made, since the publication of that statement, towards the proper evaluation of alternative methods of finance, but more research is needed to ensure that student aid policy is an effective instrument for helping to achieve a country's educational, social and economic aims.

Suggested additional reading

Edding F. 'Student Aid: Concepts, Objectives and Methods' in OECD, Financing of Education for Economic Growth. Paris: OECD, 1966, pp. 251-264.

Eide K. 'Some Financial Instruments and Efficiency Incentives in Educational Policy' in OECD, Budgeting, Programme Analysis and Cost-Effectiveness in Educational Planning, Paris: OECD, 1968, pp. 158-165.

Harris S. Higher Education: Resources and Finance. New York: McGraw Hill, 1962.

Kirkpatrick J. A Study of Federal Student Loan Programs. Washington: Government Printing Office, 1968.

Rivlin A. The Role of the Federal Government in Financing Higher Education. Washington: Brookings Institute, 1961.

Woodhall M. Student Loans as a Means of Financing Higher Education: A Review of Scandinavian Experience. Forthcoming, 1970.

Unesco/International Association of Universities: Access to Higher Education (ed. F. Bowles) Vol. 1, Appendix C, 'Direct Aid to Students'. Paris: Unesco/IAO, 1963.